No. 80-1310

APR 1

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In the Supreme Court of the United States

OCTOBER TERM, 1980

TRANSWESTERN PIPELINE COMPANY, PETITIONER

v.

FEDERAL ENERGY REGULATORY COMMISSION

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

MEMORANDUM FOR THE FEDERAL ENERGY REGULATORY COMMISSION IN OPPOSITION

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TABLE OF AUTHORITIES

Page

Cases:

Columbia Broadcasting System, Inc. v. *United States*, 316 U.S. 407 5

Ethyl Corp. v. *EPA*, 541 F. 2d 1, cert. denied, 426 U.S. 941 4

PBW Stock Exchange, Inc. v. *SEC*, 485 F. 2d 718, cert. denied, 416 U.S. 969 3

SEC v. *Chenery Corp.*, 332 U.S. 194 3

Statute:

Administrative Procedure Act, 5 U.S.C. 551(4) 3

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Petitioner contends that the court of appeals erroneously upheld the Commission's exercise of discretion in making a new rule effective prospectively.

1. Petitioner, an interstate natural gas pipeline company, sells gas for resale at rates regulated by the Federal Energy Regulatory Commission. In 1975, the company filed a rate increase, seeking to recover $9.5 million spent on unsuccessful efforts to develop a commercial-scale coal gasification project. The pipeline relied on the then current Commission regulations concerning recovery of research and development costs in rates (Pet. 7).

While this rate case was pending before an administrative law judge, the Commission issued a notice of proposed rulemaking (Pet. App. 15-31) in which it proposed to amend its regulations to provide that funds expended for commerical-scale demonstration facilities could be recov-

ered as research and development expenditures (*id.* at 17, 21). In June 1977, the Commission adopted new regulations (Pet. App. 32-77), which clarified the definition of research and development so as explicitly to permit recovery of expenditures for commercial-scale demonstration projects based on technology not yet verified as economically feasible (*id.* at 35).

The State of California sought rehearing, expressing concern that this definition might be applied retroactively to permit petitioner to include in its rates the expenditures on its coal gasification project. The Commission denied rehearing in August of 1977 (Pet. App. 84-88), stating that its new rule would have prospective effect only, and would not "be applied so as to allow retroactive rate base treatment of amounts which would not be accorded such treatment under prior definitions of R & D" (*id.* at 88).

Meanwhile, the administrative law judge had ruled against petitioner in the rate case. In June 1979, the Commission affirmed that result (Pet. App. 100-116), applying the prior regulation, which was the one in effect when the funds were expended (*id.* at 104).

On review of the final rule and the order in the rate case,[1] the court of appeals sustained the Commission (Pet. App. 1-12). The court held that the rulemaking had not irreparably injured the pipeline because it had no effect on the rate case, that the Commission had properly exercised its discretion in making the new rule prospective, and that the Commission had properly considered the old rule in disallowing the costs in the rate case (*id.* at 9-12).

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[1]The court of appeals had stayed review of the rule pending the outcome of the rate case (Pet. App. 13-14; 589 F. 2d 231 (1979)).

2. The decision of the court of appeals is correct, does not conflict with any decision of this Court or any other court of appeals, and does not warrant further review.

a. The court of appeals correctly upheld the Commission's determination that the new rule should be given prospective effect and should not reach back to ratify expenses incurred under a prior rule. This result is consistent with decisions that recognize that rulemaking ordinarily entails prospective action. See *SEC* v. *Chenery Corp.*, 332 U.S. 194, 202 (1947); *PBW Stock Exchange, Inc.* v. *SEC*, 485 F. 2d 718, 732 (3d Cir. 1973), cert. denied, 416 U.S. 969 (1974) ("rules ordinarily look to the future and are applied prospectively only * * * "). Indeed, in the Administrative Procedure Act, "rule" is expressly defined in terms of agency statements "of general or particular applicability and future effect * * *." 5 U.S.C. 551(4).

At most, the determination whether to accord retroactive or prospective effect to a new rule is one within the broad discretion of the agency. In the circumstances of this case, the court of appeals correctly ruled (Pet. App. 12) that "[t]he Commission could properly determine that an adverse effect on other parties could result from a retroactive application of the new definition," and that petitioner "has no vested right to retroactivity." At the time that petitioner embarked on the coal gasification project at issue here and when it filed a rate increase seeking reimbursement for the costs of the project, the former rule (under which the Commission has determined petitioner is not entitled to reimbursement) was still in effect. Petitioner does not—and cannot—assert that it went forward with its project on the expectation that the Commission would issue a new rule of retroactive effect explicitly allowing a utility's rates to reflect expenditures for such projects. Thus, other than being denied a windfall, petitioner has failed to show how it

has been harmed by the Commission's decision to apply its new rule prospectively. Moreover, this dispute over money spent under the old rule has no continuing significance; indeed, so far as we can determine, it may affect only one other case pending before the Commission.[2]

b. The revised definition of justifiable research and development expenditures was adopted by the Commission in response to comments by several parties in the rulemaking. Petitioner contends (Pet. 11-13) that if the revised definition at issue here were merely a clarification of the old rule it should be applied retroactively, and if, on the other hand, it were a substantive change, the Commission was required to institute a new notice and comment rulemaking before adopting the amendment. This contention is without merit.

To begin with, the Commission's amendment to the definition, which was responsive to comments to the proposed rule, did not require a new round of rulemaking. Nothing in the Administrative Procedure Act "requires new notice whenever the agency responsibly adopts the suggestions of interested parties." *Ethyl Corp.* v. *EPA*, 541 F. 2d 1, 48 (D.C. Cir.) (en banc), cert. denied, 426 U.S. 941 (1976).

Moreover, the new definition did not amount to a "clarification" of the old rule, as petitioner claims. Rather, the order "clarified" the definition of research and development to make it consistent with the new regulations, which, for the first time, recognized full-scale demonstration projects

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[2]Contrary to petitioner's contention (Pet. 13), the court of appeals' reference to petitioner's lacking the "harm necessary to reviewability" of the rule (Pet. App. 10) presents no real question of "standing". The court simply reasoned that any injury inflicted by the rule could have been rendered harmless if petitioner had prevailed in its rate case. The court did not dismiss the petition for lack of standing, but went on to review the merits of the rule, specifically finding that "the Commission acted within its discretion" in making it prospective and in considering the adverse effect on others that could flow from retroactivity (*id.* at 12).

as being justifiable research and development expenditures. As the Commission correctly concluded (Pet. App. 95) in rejecting petitioner's contention, "[i]f the recognition of such costs was not to be retroactive, certainly the concomitant revision of the definition to reflect such recognition could not be retroactive."[3]

The Commission's construction of its own regulations was plainly reasonable. The former definition included "experimental" projects only, not commercial ones. The new rule expanded the coverage and clarified the definition to make clear that commerical-scale demonstration projects would now qualify for reimbursement in rate proceedings.

Finally, despite its protestation to the contrary (Pet. 15-16), petitioner has not been treated unfairly. In the rulemaking, the Commission gave petitioner the opportunity to advance its views in a motion for reconsideration following the denial of rehearing (Pet. App. 89-99). In the rate proceeding, the Commission applied the definition of research and development that was in effect at the time of the pipeline's expenditures and found that the expenditures did not qualify for reimbursement because the project was a commercial venture and not an "experiment" within the terms of that definition.

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[3]The Commission's use of the term "clarification" in revising the definition of justifiable research and development expenditures (Pet. App. 69) did not transform its new rule into an interpretation of the old rule. It is the substance of the agency action that controls, not the label. *Columbia Broadcasting System, Inc.* v. *United States*, 316 U.S. 407, 416 (1942).

It is therefore respectfully submitted that the petition for a writ of certiorari should be denied.

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